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NO. 05-1429

IN THE

Supreme Court of the United States

TRAVELERS CASUALTY AND SURETY COMPANY OF AMERICA,

Petitioner

v.

PACIFIC GAS AND ELECTRIC COMPANY,

Respondent

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF *AMICUS CURIAE* THE SURETY & FIDELITY ASSOCIATION OF AMERICA IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI OF TRAVELERS CASUALTY AND SURETY COMPANY OF AMERICA

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STATEMENT OF INTEREST OF AMICUS CURIAE

The Surety & Fidelity Association of America ("SFAA")[1] is a trade association of companies licensed to write fidelity and surety bonds in the United States. The approximately 500 members of SFAA write the vast majority of surety bonds furnished in California and other states.

Surety bonds are provided in return for both a premium and an agreement by the bond principal to indemnify the surety against liability, loss and expense, including attorneys' fees, incurred by reason of the execution of the bonds. In the instant case, the contracts between petitioner Travelers Casualty and Surety Company of America, as administrator for Reliance Insurance Company ("Travelers")[2] and respondent Pacific Gas and Electric Company ("PG&E") obligated PG&E to indemnify Travelers for its attorneys' fees incurred in the PG&E bankruptcy. The Ninth Circuit Court of Appeals refused to

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[1] No person or entity other than The Surety & Fidelity Association of America made any monetary contribution to the preparation or submission of this Brief, and counsel for the parties did not author this Brief in whole or in part.

[2] The indemnity agreements named, and the bonds were furnished by, Travelers' predecessor in interest, Reliance Insurance Company.

enforce the attorneys' fee provisions of the indemnity contracts because the dispute between Travelers and PG&E was decided under federal bankruptcy law instead of state law.

The rule asserted by the Ninth Circuit increases a surety's risk by arbitrarily depriving it of a part of the consideration promised to induce it to furnish the bond. Indemnity agreements similar to the ones provided by PG&E are routinely required in connection with all types of surety bonds. SFAA's members are adversely impacted by the Ninth Circuit's decision.

Both Petitioner and Respondent have consented to the filing of this Brief.

SUMMARY OF ARGUMENT

The Ninth Circuit Court of Appeals rejected Travelers' argument that state law should control its claim to recover attorneys' fees incurred in protecting its rights in PG&E's bankruptcy proceeding. Even if federal law applies, however, the Ninth Circuit failed to follow this Court's precedents. The American Rule on attorneys' fees applicable in cases arising under federal law is that fees may be recovered if provided for in an enforceable

contract. Thus, the Ninth Circuit's holding was contrary to both state and federal law.

This case presents an important, recurring question that impacts a wide range of contracts in addition to indemnity agreements required in connection with all types of surety bonds. The Ninth Circuit's refusal to enforce contractual attorneys' fee provisions if federal bankruptcy law is used to decide a dispute adversely impacts parties to the many different types of contracts with attorneys' fee shifting provisions. Travelers' Petition presents an important issue that this Court should exercise its discretion to review in order to resolve a clear conflict among the circuit courts of appeal.

ARGUMENT

The Ninth Circuit Court of Appeals decision in this case[3] was that "attorneys fees are not recoverable in bankruptcy for litigating issues 'peculiar to federal bankruptcy law.'"[4] The Ninth Circuit's decision did not

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[3] *Travelers Casualty and Surety Company v. Pacific Gas and Electric Company*, 2006 WL 285977 (9th Cir. February 7, 2006). Petition Appendix page 1a.

[4] Pet. App. p.3a, quoting from *Fobian v. Western Farm Credit Bank*, 951 F.2d 1149, 1153 (9th Cir. 1991).

depend on the attorneys' fee provision of the parties' contract or on which party prevailed. The Court followed a bright line rule that parties cannot contract to shift attorneys' fees incurred litigating issues controlled by bankruptcy law.

The rule applied by the Ninth Circuit in this case and in *DeRoche v. Arizona Industrial Commission*[5] is clearly in direct conflict with decisions of other circuit courts of appeal.[6] SFAA will not repeat Travelers' explanation of the circuit conflicts. SFAA files this Brief to make two points. First, that the Ninth Circuit holding also conflicts with this Court's application of the American Rule in matters controlled by federal law,[7] and, second, that the issue presented by Travelers' Petition is an important matter which this Court should exercise its

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[5] 434 F.3d 1188 (9th Cir.2006), a Petition for Writ of Certiorari is pending in the *DeRoche* case, Case No. 05-1439.

[6] See pp. 13-15 of Travelers' Petition for a Writ of Certiorari.

[7] Supreme Court Rule 10(c), "a United States court of appeals . . . has decided an important federal question in a way that conflicts with relevant decisions of this Court."

discretion to decide in order to resolve the conflicting decisions of the circuit courts.[8]

I. The American Rule Under Federal Law Enforces Contractual Attorneys' Fee Provisions.

The Bankruptcy Code neither requires nor prohibits attorneys' fee shifting. Travelers argues that bankruptcy law recognizes a right to attorneys' fees under state law.[9] The Ninth Circuit, however, makes a distinction between issues controlled by state law and issues controlled by federal bankruptcy law. In *DeRoche*, the Ninth Circuit stated:

> However, we consistently have refused to award fees when the substantive legal question was governed by federal bankruptcy law. . . .

(434 F.3d at 1191).

In matters controlled by federal law, the American Rule is to enforce contractual attorneys' fee provisions.

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[8] Supreme Court Rule 10(a), "a United States Court of appeals has entered a decision in conflict with the decision of another United States court of appeals on the same important matter."

[9] Petition for a Writ of Certiorari at pp. 15-20.

Fleischmann Distilling Corp. v. Maier Brewing Co., 386 U.S. 714, 87 S. Ct. 1404, 18 L. Ed.2d. 475 (1967), arose under the Lanham Act. The Court stated the American Rule as:

> The rule here has long been that attorney's fees are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefor.

(386 U.S. 717, 87 S. Ct. 1407).

F.D. Rich Co., Inc. v. U.S. ex rel. Industrial Lumber Co., Inc., 417 U.S. 116, 94 S. Ct. 2157, 40 L. Ed. 2d 703 (1974), held that an action on the payment bond required by the Miller Act[10] was governed by federal law and the Ninth Circuit erred in resorting to "state policy" to award fees. This Court stated:

> The Miller Act provides a federal cause of action, and the scope of the remedy as well as the substance of the rights created thereby is a matter of federal not state law. Neither respondent nor the court below offers any

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[10] 40 U.S.C. §§ 3131, et seq.

> evidence of congressional intent to incorporate state law to govern such an important element of Miller Act litigation as liability for attorneys fees.

(417 U.S. 127, 94 S. Ct. 2164).

The Court in *F.D. Rich* also recognized that a contract's attorneys' fee provision would be enforced. The Court, citing *Fleischmann Distilling Corp.*, stated:

> We turn now to the question of whether attorneys' fees were properly awarded respondent as a successful Miller Act plaintiff. The so-called 'American Rule' governing the award of attorneys' fees in litigation in the federal courts is that attorneys' fees 'are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefor.' . . . There was no contractual provision concerning attorneys' fees in this case.

(417 U.S. 126, 94 S. Ct. 2163).

See also, *Summit Valley Industries, Inc. v. Local 112, United Brotherhood of Carpenters and Joiners of*

America, 456 U.S. 717, 721, 102 S. Ct. 2112, 2114, 72 L. Ed.2d 511 (1982)("Under the American Rule it is well established that attorney's fees 'are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefore.'"); *Hall v. Cole*, 412 U.S. 1, 4, 93 S.Ct. 1943, 1945, 36 L. Ed.2d 702 (1973)("Although the traditional American Rule ordinarily disfavors the allowance of attorneys' fees in the absence of statutory or contractual authorization. . ."); *Alyeska Pipeline Service Company v. Wilderness Society*, 421 U.S. 240, 257, 95 S. Ct. 1612, 1621, 44 L. Ed.2d 141 (1975)("Other recent cases have also reaffirmed the general rule that, absent statute or enforceable contract, litigants pay their own attorneys' fees.")

Following *F.D. Rich*, courts, including the Ninth Circuit,[11] have awarded attorneys' fees to successful Miller Act payment bond claimants if their contracts provided for fees. This is not because state law entitled them to fees. It

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[11] *United States ex rel. Reed v. Callahan*, 884 F.2d 1180, 1185-1186 (9th Cir. 1989), *Cert. Den. Esto, Inc. v. Callahan*, 493 U.S. 1094 (1990); *United States ex rel. Palmer Construction, Inc. v. Cal. State Elec., Inc.*, 940 F.2d 1260 (1991); *North Star Terminal & Stevedore Co. v. Nugget Construction, Inc.*, 126 Fed. Apx. 348, 2005 WL 487313 (9th Cir. 2005).

is because the American Rule under federal law enforces fee shifting by contract.

Thus, in the instant case, the Ninth Circuit reached a result contrary to both state and federal law. Nothing in the Bankruptcy Code forbids parties from allocating the cost of attorneys' fees by contract. California law and federal law recognize such contracts as an exception to the American Rule. If Congress wanted to forbid enforcement of contractual fee shifting in cases decided under the Bankruptcy Code, it could have done so. In the absence of such a statute, however, the Ninth Circuit is not free to legislate its own Ninth Circuit law contrary to both state law and this Court's decisions on federal law.

II. The Issue Presented by Travelers' Petition Should be Decided by This Court.

PG&E could have met its obligations to injured employees by purchasing workers compensation insurance. Instead of paying to have an insurer assume the obligations, however, PG&E chose to self-insure and pay the workers itself. Under California law, it had to provide security for

its obligations to the injured workers.[12] A surety bond was one of the permitted forms of security.[13]

Unlike an insurer, the surety on the bond did not take over primary responsibility for the benefits. PG&E remained primarily liable, and the surety merely guaranteed PG&E's performance. The risk the surety ran was that workers would be owed benefits and that PG&E would be unable to pay them.

To induce Travelers to become surety on the bonds, and thus assume a potential $100 million liability, and to keep the cost of the bonds as low as possible, PG&E executed the indemnity agreements. In Paragraph Second of the first two Agreements, PG&E promised:

> SECOND: To indemnify, and keep indemnified, and hold and save harmless the Surety against all demands, claims, loss, costs, damages, expenses and attorneys' fees whatever, and any and all liability therefor, sustained or incurred by the Surety by reason of executing or procuring the

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[12] Cal. Labor Code §3701.

[13] Cal. Labor Code §3701(d).

> execution of any said Bond or Bonds, or any other Bonds, which may be already or hereafter executed for or at the request of the Undersigned, or renewal or continuation thereof; or sustained or incurred by reason of making any investigation on account thereof, prosecuting or defending any action brought in connection therewith, obtaining a release therefrom, recovering or attempting to recover any salvage in connection therewith or enforcing by litigation or otherwise any of the agreements herein contained. Payment of amounts due Surety hereunder together with legal interest shall be payable upon demand.

(Excerpts of Record in the Ninth Circuit at pp. 41 and 45).

The third agreement stated at its second paragraph, "PG&E Corporation agrees to indemnify the Surety and hold [it] harmless in respect of any and all loss, damages, claims, costs, premiums, expenses and reasonable attorney's fees which the Surety may incur by reason of its having furnished the aforesaid Workers Compensation Bond." (Excerpts of Record at p. 51).

PG&E did not just agree to indemnify Travelers for losses paid under the bonds.[14] It also promised to indemnify Travelers for expenses, including attorneys' fees, incurred "by reason of executing" the bonds. Paragraph Second then goes on to obligate PG&E to pay any attorneys' fees incurred in connection with enforcement of the indemnity agreement. Thus, PG&E's promise to pay Travelers' attorneys' fees was not limited to actions on the indemnity contract itself. Any fees incurred by reason of the execution of the bonds were covered.

Surety bonds are required in connection with a multitude of activities including all public construction projects over a minimal size.[15] Indemnity agreements substantially similar to the ones PG&E provided Travelers are routinely obtained in connection with all kinds of surety bonds.[16] These agreements help reduce the cost of bonds

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[14] Indeed, such a promise would be largely superfluous because Cal. Civ. Code §2847 would obligate PG&E as principal on the bonds to pay Travelers for any losses.

[15] For federal construction, the Miller Act, 40 U.S.C. §§ 3131, et seq., requires performance and payment bonds. In California, Civ. Code §3247 requires payment bonds on public construction contracts.

[16] See, Klinger, et al., *The Surety's Indemnity Agreement* (American Bar Association 2002) and Shahinian, "The

and assure that any losses and expenses are paid by the bond principal or other persons or entities who agree to act as indemnitors for the principal's obligations to the surety. If bond principals do not have to live up to their promises because a dispute is decided under federal bankruptcy law instead of state law, the loss experience and costs of bonds will increase.

The same is true for other types of transactions in which attorneys' fee shifting provisions are used. If one party is obligated to pay the other party's attorneys' fees, the indemnified party can charge less for its products or services. It recovers the cost of enforcing the contract from the defaulting party. If such an indemnification provision is unenforceable, the attorneys' fees have to be factored into the cost of the products or services. Then, all parties purchasing the products or services pay an increased price. The uncollectible attorneys' fees are spread over all customers rather than being paid by the defaulting party.

In the instant case, PG&E is well able to pay Travelers' attorneys' fees, but the Ninth Circuit rule bars enforcement of the attorneys' fee provisions in the

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General Indemnity Agreement" in Gallagher, ed. *The Law of Suretyship, 2nd Ed.* (American Bar Association 2000) at pp. 487-525.

indemnity agreements. In this one instance, the consequences to Travelers' other customers may be minimal, but applied to the myriad of contracts with attorneys' fee shifting provisions, the cumulative effect of the Ninth Circuit rule is substantial and deserving of this Court's attention.

CONCLUSION

This Court should exercise its discretion to grant Travelers' Petition for a Writ of Certiorari to resolve the conflicting holdings of the circuit courts of appeal and the conflict between the holding of the Ninth Circuit Court of Appeals and this Court's controlling decisions.

Respectfully submitted,

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